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No. 93-1001

IN THE
Supreme Court of the United States
OCTOBER TERM, 1994

ALLIED-BRUCE TERMINIX COMPANIES, INC., and TERMINIX INTERNATIONAL COMPANY,
Petitioners,

v.

G. MICHAEL DOBSON, WANDA C. DOBSON, STEVEN GWIN and JAN GWIN,
Respondents.

On Writ of Certiorari to the Supreme Court of Alabama

REPLY BRIEF FOR PETITIONERS

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In construing Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, this Court does not write upon a blank slate. During the past four decades, the Court has established that "[i]n enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration." *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984); *Perry v. Thomas*, 482 U.S. 483, 489 (1987). With respect to the scope of Section 2, the Court has held that it sets forth federal substantive law enacted pursuant to the congressional power over interstate commerce (*Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967)); that it applies in state as well as federal courts (*Southland Corp.*); that

it applies not just to arbitration of disputes between merchants (*Prima Paint*) but to arbitration of a wide variety of statutory and common law claims (*e.g., Gilmer v. Interstate/Johnson Lane Corp.*, 111 S. Ct. 1647 (1991)); and that it mandates enforcement of arbitration agreements despite assertions of unequal bargaining power, unless the inequality would be grounds for the revocation of *any* contract (*Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627 (1985)).

Respondents and their *amici curiae* accept very little of this established law. Although they reluctantly concede that Congress enacted Section 2 in an exercise of its commerce power, they insist that Congress, for unexplained reasons, exercised only a fraction of that power, and they contend—urging the overruling of *Southland Corp.*—that Section 2 should not apply at all in state courts. *See* Resp. Br. at 12-14; Brief *Amici Curiae* of the Attorneys General of the State of Alabama, Alaska, et al. at 1-20 ("Ala. Br."). At various other points, they suggest that the Act should not apply to transactions with consumers and, in any event, should never apply to parties with different degrees of bargaining power. Resp. Br. at 26-28; Ala. Br. at 19; Brief *Amicus Curiae* of the Southern Poverty Law Center at 4-5 ("SPLC Br."). Then, in keeping with their general hostility towards arbitration, respondents and their *amici curiae* press for a reading of Section 2 that would limit its jurisdictional reach as much as possible, allowing States to void agreements to arbitrate unless the parties also agreed about the extent of interstate commerce involved in their transaction. Resp. Br. at 15-23; SPLC Br. at 6-11. Finally, as a fallback position, they argue that the Act should apply only to transactions in "the 'current' or 'flow' of interstate commerce," rather than to transactions generally falling within the congressional power over interstate commerce. Resp. Br. at 23-28. As we briefly discuss, however, none of these theories comfortably fits with the language of

Section 2, much less with the basic "congressional desire to enforce agreements into which the parties had entered." *Volt Info. Sciences, Inc. v. Board of Trustees*, 489 U.S. 468, 478 (1989) (quoting *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 220 (1985).

I. THE COURT SHOULD NOT OVERRULE *SOUTHLAND CORP v. KEATING.*

Although Alabama and other States (supported by respondents) urge this Court to overrule *Southland Corp. v. Keating*, and thus allow state courts to employ doctrines inimical to arbitration agreements, Ala. Br. at 1-20; Resp. Br. at 12-14, they offer nothing approaching a sufficient reason to do so. "Time and time again, this Court has recognized that 'the doctrine of *stare decisis* is of fundamental importance to the rule of law.'" *Hilton v. South Carolina Pub. Rys. Comm'n*, 112 S. Ct. 560, 563 (1991) (quoting *Welch v. Texas Dep't of Highways*, 483 U.S. 468, 494 (1987)). Noting that "[a]dherence to precedent promotes stability, predictability, and respect for judicial authority," 112 S. Ct. at 564, the Court has said that it "will not depart from the doctrine of *stare decisis* without some compelling justification." *Ibid.* The Court has further emphasized that "'[c]onsiderations of *stare decisis* have special force in the area of statutory interpretation, for here, unlike in the context of constitutional interpretation, the legislative power is implicated, and Congress remains free to alter what we have done.'" *Ibid.* (quoting *Patterson v. McLean Credit Union*, 491 U.S. 164, 172-73 (1989)). And, "[c]onsiderations in favor of *stare decisis* are at their acme in cases involving property and contract rights, where reliance interests are involved . . . ." *Payne v. Tennessee*, 111 S. Ct. 2597, 2610 (1991).

There is no "compelling justification" for departing from *stare decisis* here. To begin with, the States have given no reason why they waited 10 years—during which time thousands upon thousands of arbitration agreements

have been formed on the basis of existing law—to come forward with this point. Although they contend that they had no notice of the presence of this issue in *Southland Corp.*, saying that "the questions presented in *Southland* did not explicitly identify the Act's application to state court as the issue to be decided by this Court" (Ala. Br. at 2), they can hardly deny that the issue was necessarily present in a case involving enforcement of an arbitration agreement in state court. Moreover, they offer no explanation for their silence in *Perry v. Thomas* or *Volt Info. Sciences*, decided seven and five years ago respectively, both of which likewise involved issues about enforcement of arbitration agreements in state court. At the very least, therefore, the decision now to address the issue decided in *Southland Corp.* is highly belated.

The States (and respondents) also have little new to contribute. Having said that the Court in *Southland Corp.* "was denied the benefit of adversarial briefing on the matter" (Ala. Br. at 1), the States simply submit that "Justice O'Connor's dissent in *Southland* . . . is demonstrably correct and should be adopted by this Court as the proper interpretation of the FAA." Ala. Br. at 2. This suggestion seems little more than a plea to overrule a prior considered decision on the basis of a change in composition of the Court. The doctrine of *stare decisis* itself, however, reflects the principle that existing law should not commonly be set aside simply to reflect changes in the membership of the Court. *See, e.g., Florida Dep't of Health & Rehabilitative Servs. v. Florida Nursing Home Ass'n*, 450 U.S. 147, 153 (1981) (Stevens, J., concurring); *Mapp v. Ohio*, 367 U.S. 643, 677 (1961) (Harlan, J., dissenting).

Nor have events since the decision in *Southland Corp.* cast doubt upon its basic premises. Although the States say that the decision in *Volt Info. Sciences* has "undercut" *Southland Corp.*, Ala. Br. at 3, that is wishful thinking on their part. The Court in *Volt* did not question

that state courts have an obligation, under Section 2, to enforce arbitration agreements according to their terms: it simply made clear that, as part of those terms, the contracting parties could agree to be bound by certain provisions of state law. Given that "the federal policy is simply to ensure the enforceability, according to their terms, of private agreements to arbitrate" (489 U.S. at 476), and given that "parties are generally free to structure their arbitration agreements as they see fit" (*id.* at 479), the Court merely recognized that courts—whether state or federal—should ordinarily give effect to the parties' own intentions about how to arbitrate their claims. Nothing in that decision states, or even implies, that state courts should be free to do the opposite: disregard the stated agreement of the parties on the basis of legislative or judicial hostility towards agreements to arbitrate.

Finally, the States argue that Section 2 (as construed in *Southland Corp.*) infringes upon their sovereign rights to regulate contracts and protect consumers and that it lacks a clear enough statement of congressional intent to do so. Ala. Br. at 8-9. But this argument has a number of flaws. First of all, if the States mean to say that Section 2 fails to preempt state laws hostile to arbitration, then it would follow that Section 2 is inapplicable even in *federal* court, at least when state law typically provides the substantive law. As a general rule, the power of states to regulate contracts does not come and go depending on the forum in which suit is brought, yet the States make no attempt to explain why their theory leaves off at state courts. Moreover, and in any event, their argument against preemption of anti-arbitration laws is foreclosed by the fact that Congress *did* make a clear statement with respect to enforcement of arbitration agreements: those agreements are "valid, irrevocable, and enforceable" to the same extent as other contracts. And, by specifically providing that contracts to arbitrate could be held invalid "upon such grounds as exist at law or in equity for the revocation of any contract," 9 U.S.C. § 2, Congress left

little room for States to argue, as they do here, that Section 2 also allows for revocation of arbitration agreements based on nothing more than a dislike of arbitration agreements generally.

II. THE SCOPE OF SECTION 2 DOES NOT DEPEND UPON THE PARTIES' AGREEMENT ABOUT THE EXTENT OF INTERSTATE COMMERCE INVOLVED IN THEIR TRANSACTION.

To provide context for the arguments made by respondents and their *amici curiae* with respect to the scope of Section 2, it is worth setting out what they do not contest. First, despite some grumbling, they do not dispute that respondents entered into a written agreement to arbitrate disputes arising out of the termite protection plan with petitioners. Resp. Br. at 2-3. Furthermore, they do not dispute that, were it not for the specific Alabama policy disfavoring arbitration agreements, this agreement would be fully binding as a matter of state law: that is, nothing in the agreement would be grounds for revocation of *any* contract under state law. Nor do they deny that the materials used to treat respondents' home—the principal obligation undertaken by petitioners pursuant to the contract —moved in interstate commerce. *Id.* at 7. And they necessarily accept that Congress has the power to make the arbitration agreement "valid, irrevocable, and enforceable" as a matter of substantive federal law.

Respondents nevertheless urge a reading of Section 2 that would allow them to walk away from their agreement to arbitrate (while continuing to press their claims for damages under the same contract), giving full play to state law disfavoring agreements to arbitrate. The linchpin of this argument is that the words "a contract evidencing a transaction involving commerce" require that the contract explicitly reflect the interstate elements of the transaction (and, thus, demonstrate the "contemplation" by the parties of "substantial interstate activity"). *See* Resp. Br. at 15-20. But this reading, while perhaps not unimaginable, is certainly unnatural. Given that the words

"transaction involving commerce" (like the words "maritime transaction") are plainly intended to mark out the jurisdictional bounds of the statute, it would be extremely odd to have made the presence or absence of jurisdiction turn on the parties' understanding about the jurisdictional facts, rather than on the facts themselves. Reading the words together, therefore, it seems most natural to think that Congress imposed two related, but distinct, requirements: to establish a jurisdictional nexus, there must be a "transaction involving interstate commerce" and, to assure that the agreement to arbitrate relates to that transaction, there must be a contract (containing a written agreement to arbitrate) "evidencing" the transaction. Those conditions having been satisfied, it is difficult to understand what difference it should make that the parties do or do not set forth the interstate elements of the transaction in the contract.

Respondents attempt to address this point by saying that the Act is intended to carry out the "expectations" of the parties. Resp. Br. at 17. But, here, respondents are mixing apples and oranges. It is correct, indeed fundamental, to say that the Act seeks to advance the parties' "expectations" *about arbitration*, but that is very different from saying that the scope of the Act turns on the parties' "contemplation" *about interstate commerce*. Thus, while this Court has repeatedly recognized that Section 2 comes into play only after contracting parties have agreed to submit disputes to arbitration, *see, e.g., Volt Info. Sciences*, 489 U.S. at 476, it has never suggested that the parties must also agree about the extent of interstate commerce involved in their transaction. Provided that the agreement to arbitrate exists, as it does here, Section 2 operates to make that agreement enforceable so long as the necessary jurisdictional grounds (a "maritime transaction" or "a transaction involving commerce") have been met.

Respondents' argument would be more compelling, of course, if there were some basis to think that the parties'

expectations about arbitration were tied to their expectations about interstate commerce. But respondents do not put forward any such argument, and for good reason. To adopt that theory, it would be necessary to believe that parties enter into written agreements to arbitrate while secretly anticipating that (for want of adequate interstate activity) state law will be deemed to apply and make their agreement effectively meaningless. Quite apart from the fact that this speculation is implausible, it supposes a roundabout, if not actively deceitful, way of evading arbitration, and it is hardly likely that Congress meant to encourage it. Thus, insofar as a meeting of the minds is concerned, it is only the agreement to arbitrate, not an agreement about interstate commerce, that the Act requires.[1]

The reasoning employed by Judge Lumbard, heavily relied on by respondents (*see* Resp. Br. at 15-19), is similarly unpersuasive. Rejecting the view (adopted by the Second Circuit in an earlier case) that "Congress intended to use to the fullest possible extent its powers to regulate commerce as it was affected by arbitration agreements," *Metro Indus. Painting Corp. v. Terminal Constr. Co.*, 287 F.2d 382, 386 (2d Cir.), *cert. denied*, 368 U.S. 817 (1961), Judge Lumbard instead concluded that "we must be cautious in construing the act lest we excessively encroach on the powers which Congressional policy, if not the Constitution, would reserve to the states." *Ibid.* But this "cautio[n]" leads Judge Lumbard to the same error that respondents make: in deliberately seeking grounds to narrow the reach of the Act, he mixes together the understanding of the parties regarding arbitration with their understanding regarding interstate commerce to pro-

[1] We note that the origin of the language "contract evidencing a transaction involving commerce" fully supports the notion that Congress was tailoring the Act to the extent of its legislative powers. *See* Pet. Br. 15-16. Neither respondents nor their *amici curiae* have any response to this point.

duce a limitation not reasonably derived from the statute.[2] Thus, while he is entirely correct in saying that Congress did not intend to impose arbitration on those who had not agreed to it, he is incorrect in deciding that those who have agreed to it—and done so in contracts dealing with transactions involving interstate commerce in fact—may be permitted to avoid their obligations based on later claims that they did not "contemplate" the interstate activity involved.

We submit, therefore, that the "contemplation-of-the-parties" test has no place in the application of Section 2, even if that section were to be construed without any regard for the policies underlying the Act. But we note that respondents make no effort to explain why, even though "questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration" (*Gilmer*, 111 S. Ct. at 1652 (internal quotes omitted)), questions about the scope of Section 2 should not. If anything, it would seem that federal policy should play a *greater* role in construction of the *Act*, which reflects the intent of Congress itself, than in construction of arbitration agreements, which reflect the intent of the contracting parties. And, given that Congress had, as its primary intention, to make voluntary agreements enforceable, it is sensible to think that Congress would wish to apply that policy fully throughout the fields that it marked out.

The "contemplation-of-the-parties" test also seems to raise more problems than it solves. Described by respondents as "largely objective" (Resp. Br. at 21), and by one *amicus curiae* as "objective, not subjective" (SPLC Br. at 7), the test is, in fact, mostly unfathomable. As an initial matter, it invites a cumbersome inquiry into the

[2] Indeed, Judge Lumbard ultimately works backwards in construing the statute, saying that "[t]he rule of construction should be based on some more realistic appraisal of the ends Congress wished to serve." 287 F.2d at 387.

subjective understandings of the parties about the nature of the transaction and any interstate activity likely associated with it. Although the contract itself would be evidence of the parties' "contemplation," there is no obvious basis for limiting the inquiry to the contract rather than allowing either party to argue that it does not fully reflect the understood nature of the transaction. Moreover, in the case of contracts assumed by successor parties (like the one involved here), the inquiry would be further complicated by the need to examine the understandings of the *original* parties, unless a previously binding agreement were to become voidable simply because the successors (or, perhaps, one successor) to the contract did not also "contemplate" substantial interstate activity. With so much ambiguity unresolved, the test seems especially prone to case-by-case manipulation in the hands of courts wishing to avoid the federal directive to enforce arbitration agreements.

Finally, citing a handful of cases, respondents make the argument that "[t]he 'contemplation of the parties' test is also perfectly consistent with Congress' understanding of background Commerce Clause jurisprudence when the Act was passed in 1925." Resp. Br. at 22. But the cases are not at all on point,[3] and, anyway, there is no indica-

[3] Two of the cited cases—*Cincinnati, Portsmouth, Big Sandy, & Pomeroy Packet Co. v. Bay*, 200 U.S. 179 (1906) and *Binderup v. Pathe Exchange, Inc.*, 263 U.S. 291 (1923)—involve combinations or conspiracies to restrain interstate commerce under the Sherman Act. This Court had observed at the time that, to demonstrate an unlawful conspiracy or combination, *"the intent to injure, obstruct, or restrain interstate commerce* must appear as an obvious consequence of what is to be done, or be shown by direct evidence or other circumstances." *United Mine Workers v. Coronado Coal Co.*, 259 U.S. 344, 408 (1922) (emphasis added). Even respondents do not contend that the FAA incorporates any such standard. The third case—*Kansas City Structural Steel Co. v. Arkansas*, 269 U.S. 148 (1925)—though noting that local transactions were "contemplated," was decided, not on that basis, but on the basis of *actual* local activities. *See id.* at 152 ("the things *done* by the plaintiff in error in Arkansas . . . constitute or include intrastate business") (emphasis added).

tion that Congress had them in mind at the time. In contrast, a brief submitted as part of the legislative record explicitly informed Congress that its powers over interstate commerce "govern every agency or act which bears so close a relationship to interstate commerce that they can reasonably be said to affect it" and that "[c]ontracts relating to interstate commerce are within the regulatory powers of Congress." *See* Joint Hearings on S. 1005 and H.R. 646 Before the Subcomm. of the Comms. on the Judiciary, 68th Cong., 1st Sess. 38 (1924) (Brief submitted by Julius H. Cohen, member of the Committee on Commerce, Trade & Commercial Law of the ABA and the General Counsel for the N.Y. State Chamber of Commerce). In light of the fact that the relevant House Report tracks this language ("contracts relating to interstate commerce") in describing the scope of the commerce power, H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924), it is fanciful to attribute to Congress an intent to rely on the "contemplation" of the parties in setting the jurisdictional bounds of the Act.

III. THE "FLOW" OR "CURRENT" OF INTERSTATE COMMERCE TEST SHOULD NOT BE READ INTO SECTION 2.

Respondents argue that, in any event, Congress did not intend to use its commerce powers to the fullest, but rather meant to reach only transactions by merchants in the "flow" or "current" of interstate commerce. This Court, of course, has said just the opposite. *See Perry*, 482 U.S. at 490 (Act "embodies Congress' intent to provide for the enforcement of arbitration agreements within the full reach of the Commerce Clause"). While that statement is not controlling, it does reflect an understanding of the Act reached by a number of other courts. *See, e.g., Foster v. Turley*, 808 F.2d 38 (10th Cir. 1986); *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271

F.2d 402, 407 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960). Respondents' efforts to disprove it are singularly unimpressive.

The principal argument advanced by respondents is that, to validate the statement in *Perry*, the Court would have to overrule *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198 (1956). Resp. Br. at 11, 20. But, in taking that position, respondents utterly ignore the test actually employed by this Court in *Bernhardt*: whether "[the employee] while performing his duties under the employment contract was working 'in' commerce, was producing goods for commerce, or *was engaging in activity that affected commerce*, within the meaning of our decisions." 350 U.S. at 200-01 (emphasis added). The last part of that test plainly reflects the broad extent of powers granted to Congress under the Commerce Clause, without limiting the inquiry to the "flow" or "current" of interstate commerce. While one can fairly question whether the facts of the case fell within or without this test, it is totally off-the-mark to say that *Bernhardt* established that, in enacting Section 2, Congress called upon only a fraction of its powers under the Commerce Clause.

Respondents then submit that "the phrase 'a transaction involving commerce' should be defined to mean a transaction between businesspersons who are part of the 'flowing stream' of commerce as the term 'commerce' was understood in 1925." Resp. Br. at 26. But this Court has already rejected the argument that Section 2 applies only to dealings between merchants. *See Prima Paint*, 388 U.S. at 401 n.7. Moreover, businesspersons aside, it is simply mistaken to assert that, in 1925, the power of Congress to regulate interstate commerce was limited to "a flowing stream from one State to another formed by a regular course of business." Resp. Br. at 26. As one case cited by respondents itself makes clear, "if Congress deems certain recurring practices though not really part of interstate commerce, likely to obstruct, restrain, or burden it, it has the power to subject them to national supervision

and restraint." *United Mine Workers v. Coronado Coal Co.*, 259 U.S. 344, 408 (1922). That view, as we have already noted, corresponds closely to the contemporaneous views put before Congress regarding the extent of its powers to regulate commerce. *See* page 11 *supra*.

The existence of a power to regulate, of course, is not conclusive on the question whether Congress exercised it. Respondents and their *amici curiae*, however, have offered little reason to suppose that Congress did not. One *amicus curiae* argues that, in the absence of a narrowing construction, "[f]ederal law would . . . guarantee landlords, television repair shops, dry cleaners, and every other local business the right—regardless of their highly attenuated connection to interstate commerce—to insert clauses into their form contracts waiving consumers' rights to a judicial forum." SPLC Br. at 3. But, quite apart from the threshold requirement of a written agreement to arbitrate—thus eliminating most casual consumer transactions—it is well recognized that a "highly attenuated connection to interstate commerce" is not enough to fall within the boundaries of the Commerce Clause. To the contrary, the Court has recognized that the exercise of the commerce power cannot be extended to "effects upon interstate commerce so indirect and remote" (*NLRB v. Jones & Laughlin Steel Co.*, 301 U.S. 1, 37 (1937)) that the distinction between local and national activities would be lost. Where the nexus is more substantial, however, we see no reason why parties should not be able to make binding agreements to arbitrate disputes about the purchase of television sets or the sale of services to local consumers.[4]

[4] The service purchased here, in a written contract between parties in different States, involved the direct application of materials brought into Alabama from out-of-state in order to perform that service. Such transactions, like the direct sales of goods moving in interstate commerce, seem well within the outer boundaries of those commercial dealings that, taken in the aggregate, have a substantial effect on interstate commerce. *See, e.g., Fry v. United*

The attempts by respondents and their *amici curiae* to narrow Section 2 appears to reflect a concern that consumers lack the bargaining power to resist agreements to arbitrate. Resp. Br. at 11-12; Ala. Br. at 19; SPLC Br. at 12. That this is so is certainly not a foregone conclusion: neither respondents nor their *amici curiae* have demonstrated that consumers willing to pay higher costs for a product or service cannot bargain to eliminate any agreement to arbitrate. But, in any case, this Court has repeatedly rejected arguments that Section 2 does not apply to persons of unequal bargaining power. *See Gilmer*, 111 S. Ct. at 1655-56; *Mitsubishi Motors*, 473 U.S. at 627. The proper question, as the Court has made clear, is not whether the parties have different levels of bargaining power but whether any inequality is "grounds . . . for the revocation of any contract." 9 U.S.C. § 2. If the inequality of bargaining power is not enough to invalidate other obligations, then a state hostile to arbitration may not single it out as a basis for voiding an agreement to arbitrate. Thus, while a State retains full power to protect its citizens against adhesion contracts, it may not establish special, discriminatory standards disfavoring arbitration agreements. Section 2 puts contracts to arbitrate "upon the same footing as other contracts," *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 511 (1974), no more and no less.

States, 421 U.S. 542, 547 (1975); *Perez v. United States*, 402 U.S. 146, 154 (1971).

CONCLUSION

The judgment of the Supreme Court of Alabama should be reversed.

Respectfully submitted,

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